NOTES

THE RECENT BOND ISSUES

On November 18, 1907, Mr. Cortelyou, secretary of the treasury, issued two circulars, one asking bids for $50,000,000 of the 10-30 Panama Canal Loan, authorized June 9, 1902, bearing 2 per cent. interest and available to national banks as security for note issues; the other, for $100,000,000, 3 per cent. certificates of indebtedness, authorized June 13, 1898, in denominations of $50, payable to bearer, redeemable November 20, 1908, and in appearance resembling ordinary paper money. The funds from the sale of Panama bonds were not yet needed for the work on the canal. The 3 per cents. were authorized during the war with Spain to enable the treasury to obtain funds "in time of need." The issue of both at that time was part of the supposed scheme to relieve the money market. The objections to these issues for the purpose alleged are obvious and conclusive:

1. The lending power of the banks depended on filling up their depleted reserves; and only by lending could the business public be kept from ruin. While reserves were being drawn off by calls from the interior, they were anxiously importing gold from Europe. At this critical juncture, the Treasury sold bonds, which demanded, in the first instance, a payment from the bank reserves of at least 25 per cent. of the bonds purchased. Instead of a help this was another drain on the banks, which were asked patriotically not to let the government loan fail.

2. Even though the government wished the banks to carry the remaining 75 per cent. of the subscription to the sub-treasury, on the understanding that it would be returned the same day on deposit, the banks would have lost to the treasury the 25 per cent. in cash. And, unless the banks could obtain suitable securities, other than United States bonds, to leave with the treasury to protect the deposit of the 75 per cent., they would have had to use the bonds just purchased for that purpose. Hence, these bonds could not have been used as security for note-issues. And this is what would have happened in places like Chicago, in the West,

where the savings-bank bonds of eastern states (accepted by the treasury as security for government deposits) could not be bought quickly.

3. But, even in New York, where other securities than United States bonds could be had, and offered as security for government deposits, the new bond issues could not help in adding to the circulation within a time which would affect the existing crisis. After being bought, it would be necessary to send the bonds to Washington, where there would have been delay because of an overburdened clerical force; then there would be more delay in getting the notes printed from the plates of the individual bank, which, in the present capacity of the public engraving bureau would be weeks, or months. In short, the notes based on those new bonds might possibly be issued by next spring, long after the crisis had passed. And, when issued, the banks would know that they could not be withdrawn easily, under the existing law, which forbids the retirement of more than $9,000,000 in any one month. Meanwhile, the banks would be without the use of the 25 per cent. paid out of their cash reserves.

4. Moreover, if the banks could have issued their own notes quickly, these notes could not have been used to fill up their reserves; and their power to lend would not have been increased. They could have paid out their own notes to state banks and correspondents, other than national banks, which could have used them as reserves. Thus, bank notes would have been of considerable service in obtaining lawful money, and in preventing lawful money from being drawn from reserves; but only in this indirect manner would bank issues have aided the power of the banks to lend.

5. Again, on what legal grounds could the treasury have claimed that a "time of need" existed, and have issued the 3-per-cent. certificates of 1898, when there was a free balance of $242,-000,000 belonging to the government? It would be no defense to say that almost all of this free balance was deposited with the banks, and could not be called upon without crippling business. This was not the condition of "need" contemplated by the statute. Moreover, the selling of those certificates to the banks necessitated withdrawals of cash from the banks. Then, if the treasury was in need, why not have called directly on some of its deposits with the banks? That would have hurt the banks no more.

6. It might have been thought that the offer of 3-per-cent.

certificates would have furnished a tempting investment to those who were hoarding money, withdrawn by runs on the banks, and thus have enabled the treasury to return the sums to the banks as deposits. This theory was belied by the facts. In the first place, banks in the country districts were hoarding large sums, as a protection against the unexpected; business men getting cash receipts did not deposit with the banks, because they could not get the cash back from the banks again. The runs on the banks outside of New York City by small depositors were very slight. And those who might have bought government bonds had knowledge enough to enable them to buy securities in the open market yielding 8 to 10 per cent. The number of those who became new shareholders of great companies in small amounts was surprisingly great; and showed that popular subscriptions to low-priced government bonds would have been insignificant. In fact, bonds bearing such low interest would be salable chiefly to national banks wishing to increase their circulation.

7. The worst feature of the confused state of mind at Washington was the use of the old fallacy of "greenbackism" that the prosperity of the country was dependent upon the volume of the circulating medium. The venerable per-capita sophistry came into play, and the increase of the currency was heralded as a desirable consummation. Such expressions go to show a complete ignorance as to the cause of the financial stringency. The banks were unable to lend freely because their depositors drew out lawful reserves; and because many of their loans were based on doubtful transactions.

8. The tendency to ask the government to take chestnuts out of the fire for private interests is too apparent in these transactions. The deposit of government funds with the banks, especially if a rate of interest were charged, has much to be said in its favor. It may properly be said, in view of our rigid and inelastic currency, that deposits by the government were the quickest, and only, way by which the ability of the banks to lend, and to save the commercial world, could be supported. This would hold true, however, only if the loans of the banks were all of a legitimate kind, and were free from the taint of unsound promotions. It is dangerous to lead the money market to expect help from the treasury when in straits and it is a dangerous position in which to expose a secretary of the treasury.

As to the real purpose of the above issues, there are several explanations. Most obviously, they were intended to serve, according to the lingo of the advertisers, as "window-dressing." That is, the administration had the political bad luck to have a financial crisis occur while the Republican party was in power, and, while a high tariff existed, contrary to all promises when asking for support in previous campaigns, that the party and the tariff would insure industrial prosperity. Seeing that the banks must very soon return to normal conditions, by their own means, the politicians at Washington made a flashy bid for the ignorant vote, on the ground that the bond issues would increase the circulation, and restore confidence. The administration impetuously attempted the impossible, either through ignorance, or too much confidence in the effects of a "bluff."

But more than this, the recent bond issues seem to indicate a panic in official circles. It is inconceivable that the plan could have been recommended by any experienced banker, or by the secretary himself. There is good reason to believe that it was a policy conceived only in the fertile mind of some high official who had no knowledge of banking. And it is not hard to guess that it was solely a political measure, intended for popular consumption. The sudden falling off in the revenues must have created consternation at the possibility of being unable to meet warrants on the treasury with a diminishing income, when the large free fund was practically locked up in the banks. Such an event would have spelled political ruin in the coming presidential election. Certainly this transaction is the most unsatisfactory financial performance since the silver legislation; and the evident desire to escape from the blunder is disclosed in the reduction of the allotments of the 3 per cents. to $15,000,000, and a large reduction in the allotments of the Panama bonds.

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THE WORKING OF RESTRICTED CREDIT

Taking it to be true that the commercial crisis is a phenomenon of the contraction of credit, it nevertheless remains to inquire as to the sense in which this is true. Is it either primarily or exclusively a contraction of bank credit, or rather a contraction of credit